

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF MONTANA**

In re

PAIGE SCARLETT O'DOWD,

Debtor.

Case No. **04-62325-7**

MEMORANDUM OF DECISION

At Butte in said District this 2nd day of February, 2005.

In this Chapter 7 bankruptcy, after due notice, a hearing was held December 7, 2004, at Butte, on the Motion to Modify Stay filed by Gallatin Valley Furniture Co. ("GVF") on October 29, 2004. Attorney W. Lee Stokes, of Bozeman, Montana, appeared at the hearing on behalf of GVF and in support of the Motion to Modify Stay. Attorney James J. Screnar, of Bozeman, Montana, appeared at the hearing on behalf of Debtors and in opposition to GVF's Motion to Modify Stay. The Chapter 7 Trustee filed a consent to GVF's Motion on November 1, 2004, and thus did not participate in the hearing. Jim Decosse ("Jim") of GVF testified, as did Debtor, and GVF's Exhibit 1 and Debtor's Exhibit A were admitted into evidence without objection. This memorandum contains the Court's findings of fact and conclusions of law.

In June of 2003, Debtor began purchasing furniture, draperies and other such items from GVF. Debtor's purchases totaled approximately \$52,000.00. GVF delivered approximately \$38,000.00 worth of the items to Debtor's home and the balance of the items remain in GVF's possession. Jim testified that \$13,000.00 worth of the items delivered to Debtor's home are custom items that no longer have a value to GVF.

GVF asserts in its Motion that the balance owing on Debtor's account is \$31,428.19 while Debtor maintains that she has paid GVF roughly \$21,758.77 toward her purchases of \$52,000.00. GVF applied the payments made by Debtor first to the custom items and then to the remainder of the items purchased. Jim testified that GVF could in theory realize about \$22,000.00 from the sale of the items in Debtor's possession and the items still in GVF's possession.¹

Debtor does not oppose GVF's motion as it relates to the items still in GVF's possession and further agrees that GVF has a valid security interest in the items of furniture still in GVF's possession. Given Debtor's position on the valid security interest in the items still in GVF's possession and pursuant to Montana statutory law, the Court concurs with Debtor's position. *See* MONT. CODE ANN. ("MCA") §§ 30-9A-110 and 30-9A-313(1). Debtor, however, opposes GVF's motion as it relates to the items in Debtor's possession. Debtor's opposition is premised on the fact that the items in Debtor's possession were delivered either in December of 2003, or prior to that date. However, it was not until March 8, 2004, that GVF had Debtor sign a promissory note for the items purchased. GVF proceeded to file a UCC-1 statement with the Gallatin County Clerk and Recorder, on March 9, 2004.

The commencement of a case under the Bankruptcy Code generally stays any and all proceedings against debtors. 11 U.S.C. § 362(a); *Christensen v. Tucson Estates, Inc. (In re Tucson Estates, Inc.)*, 912 F.2d 1162, 1166 (9th Cir. 1990). The importance of the automatic stay is discussed in the legislative history of § 362:

¹ GVF's motion similarly provides that GVF's collateral has a fair market value of \$22,698.

The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.

H.R.Rep. No. 95-595, 95th Cong. 1st Sess. 340-42 (1977); S.Rep. No. 95-989, 95th Cong., 2d Sess. 54-55 (1978); *reprinted in* 1978 U.S.Code Cong. & Admin. News 5787 at 5840-41 and 6296-97.

The fundamental debtor protections afforded by § 362(a), however, are not absolute. 11 U.S.C. 362(d). As explained in § 362(d):

On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest[.]

Except for the issue of a debtor's equity in property, in a proceeding on a motion to modify the automatic stay, the debtor has the burden of proof to show that the stay should not be modified or annulled. *In re National Env'tl. Waste Corp.*, 191 B.R. 832, 836 (Bankr. C.D.Cal. 1996), *aff'd*, 129 F.3d 1052 (9th Cir. 1997); *In re Syed*, 238 B.R. 126, 132 (Bankr. N.D.Ill. 1999); *In re Sauk Steel Co., Inc.*, 133 B.R. 431, 436 (Bankr. N.D.Ill. 1991); 11 U.S.C. § 362(g).

As noted above, § 362(d)(1) allows a court to grant relief from the automatic stay for cause. In *In re Westco Energy, Inc.*, 18 Mont. B.R. 199, 211 (Bankr. D.Mont. 2000), this Court explained the standard for modifying the stay for “cause” under § 362(d)(1):

Section 362(d), however, provides that, “[o]n request of a party in interest and after notice and a hearing, the court shall grant relief from the [automatic] stay” in three instances. The subsection relevant to these proceedings is § 362(d)(1), which allows for the granting of relief from the automatic stay “for cause”. What

constitutes cause for purposes of § 362(d) “has no clear definition and is determined on a case-by-case basis.” *Tucson Estates*, 912 F.2d at 1166. *See also Little Creek Dev. Co. v. Commonwealth Mortgage Corp. (In the Matter of Little Creek Dev. Co.)*, 779 F.2d 1068, 1072 (5th Cir. 1986) (Relief from the automatic stay may “be granted ‘for cause,’ a term not defined in the statute so as to afford flexibility to the bankruptcy courts.”).

The bankruptcy court’s decision on a motion for relief from the automatic stay is subject to the discretion of the court, and is subject to review for an abuse of discretion. *In re Leisure Corp.*, 234 B.R. 916, 920 (9th Cir. BAP 1999).

With regard to the items of property at issue, MCA § 30-9A-201 provides: “Except as otherwise provided in chapters 1 through 9A, a security agreement is effective according to its terms between the parties”. Pursuant to MCA § 30-9A-203, “a security interest is enforceable against the debtor and third parties with respect to the collateral only if: (a) value has been given; (b) the debtor has rights in the collateral or the power to transfer rights in the collateral to a secured party; and (c) one of the following conditions is met: (i) the debtor has authenticated a security agreement that provides a description of the collateral[.]”

Based upon the testimony of Debtor and the arguments of her counsel, it is obvious that Debtor does not dispute that value has been given or that Debtor has rights in the collateral. At issue is whether Debtor has authenticated a security agreement that provides a description of the collateral. The Bankruptcy Appellate Panel of the First Circuit has recognized that under the Uniform Commercial Code:

[T]here is no magic language required to constitute a security agreement. “A writing or writings, regardless of label, which adequately describes the collateral, carries the signature of the debtor, *and establishes that in fact a security interest was agreed upon*, [satisfies] the formal requirements of the statute and the policies behind it.”

In re Esteves Ortiz, 295 B.R 158, 164 (1st Cir. BAP 2003) (emphasis in original).

Debtor acknowledges that her signature appears on both the promissory note and the UCC-1 Financing Statement. Additionally, MCA § 30-9A-108(1) states that “a description of personal . . . property is sufficient, whether or not it is specific, if it reasonably identifies what is described. MCA § 30-9A-108(2) clarifies that “a description of collateral reasonably identifies the collateral if it identifies the collateral by: . . . any other method, if the identity of the collateral is objectively determinable.”

As previously noted, Debtor signed both the promissory note and the UCC-1 Financing Statement. The promissory note makes reference to the “Form UCC-1 for merchandise delivered to date”. The UCC-1 Financing Statement signed by Debtor, and filed by GVF with the Gallatin County Clerk and Recorder², specifically identifies all items of collateral. Therefore, the Court finds that the identity of the collateral is “objectively determinable” as required by MCA § 30-9A-108.

Thus, the remaining issues before this Court are whether the promissory note and financing statement constitutes a security agreement between the parties and whether such agreement creates or provides for a security interest in the merchandise. Debtor testified that she felt pressured by GVF to sign the promissory note and that she did not fully understand what she was signing. She did not request the assistance of an attorney for purposes of reviewing any documents prior to signing the promissory note and financing statement. Debtor testified that she

² The purchase-money security interest in the consumer goods attached and was perfected without any filing pursuant to MCA § 30-9A-309(1), although the creditor may elect to file. Filing a financing statement is necessary to perfect a non-purchase-money security interest in consumer goods. *See* 30-9A-320(2).

made various payments to GVF through November of 2003 on the items purchased. Debtor admittedly did not make any payments in December of 2003 or January and February of 2004. Jim thus contacted Debtor and asked that she “come in” and sign a note. Debtor complied with Jim’s request by going to GVF on March 8, 2004, and signing both the promissory note and the UCC-1 Financing Statement, which had been prepared by personnel at GVF. Pursuant to the terms of the promissory note, Debtor also made a payment of \$3,000.00 on March 8, 2004. The promissory note that Debtor signed provides in pertinent part in the last paragraph: “Security interest will be filed at Court House on Form UCC-1 for merchandise delivered to date and security interest shall be retained on merchandise in storage. Merchandise shall remain in storage till paid in full. [GVF] shall have immediate access to secured merchandise for purpose of recovery of amount due should any payment be not made in a timely manner as state above.”

Under the revised Uniform Commercial Code, a “‘security agreement’ means an agreement that creates or provides for a security interest.” MCA § 30-9A-102(uuu). An “‘agreement’ means the bargain of the parties in fact as found in their language or by implication from other circumstances, including course of dealing or usage of trade or course of performance” MCA § 30-1-201(3). A “‘security interest’ means an interest in personal property or fixtures that secures payment or performance of an obligation.” MCA § 30-1-202(37)(a). In bankruptcy, state law governs security interests in property. *Butner v. United States*, 440 U.S. 48, 55, 99 S.Ct. 914 (1979). The revised Article 9 provisions of the Uniform Commercial Code apply as this case was filed on July 28, 2004, after the Article 9 revisions, which became effective date of July 1, 2001. *See In re Wiersma*, 283 B.R. 294, 299 (Bankr. D. Idaho 2002).

“Case law [on the issue of what creates or provides for a security interest] under old

Article 9 should continue to apply under the revision, bearing in mind that Revised Section 9-203 requires an authenticated record rather than a signed writing.” 1 Coogan, SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE 2004, §2A.04, p. 2A-29. The Montana Supreme Court in *Wagner v. Glasgow Livestock Sales Co.*, 222 Mont. 385, 390, 722 P.2d 1165, 1168 (1986) confirms the requirements for the enforcement of a security agreement under the old MCA § 30-9-203, which are consistent with the requirements of the revised MCA § 30-9A-203(2), except for the distinction between an authenticated record and a signed writing.

Nowhere in either Former Article 9 or Revised Article 9 is there a requirement that a security agreement contain language “granting” the secured party a security interest. While there are some courts that have held that granting language is required in a security agreement, the prevailing rule is that while no “magic words” are required, the writings, taken together, must demonstrate an intent on the debtor's part to create a security interest in the collateral. [footnotes omitted].

Juliet M. Moringiello, *Revised Article 9, Liens from the Fringe, and Why Sometimes Signatures Don't Matter*, 10 Widener J. Pub. L. 135, 154-55 (2001). *See also* Wiersma, 283 B.R. at 306, citing *Simplot v. Owens*, 119 Idaho 243, 805 P.2d 449 (1990) (the words “SECURITY: 1956 GMC bus” and delivery of the certificate of title to creditor created a security interest). “In addition, the court [in *Owens*] observed that no special words are necessary to create a security interest, . . . that form [should] not prevail over substance and that, whenever possible, effect should be given to the parties' intent. Given this instruction, the touchstone question in determining if a security interest was created [or provided for] is whether the transaction was intended by the parties to have the effect of giving security.” Wiersma, 283 B.R. at 306. Also “a security agreement does not have to consist of a single writing. The necessary elements may appear in several writings, provided they are tied together as relating to the same transaction and

the debtor signs each.” 1 Coogan, SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE 2004, §2A.04[2][a], p. 2A-31-32. The several writings theory is better known as the “composite document” theory derived from the analysis undertaken by the court in *In re Numeric Corp.*, 485 F.2d 1328 (1st Cir. 1973) and followed by many courts, including *Matter of Bollinger Corp.*, 614 F.2d 924, 927 (3rd Cir. 1980). In *In re Ace Lumber Supply, Inc.*, 7 Mont. B.R. 500, 105 B.R. 964, 967 (Bankr. D. Mont. 1989), Judge Peterson concluded “under Montana law the composite document rule is available to provide evidentiary support to create a security [interest] in collateral. *Ace Lumber Supply*, 105 B.R. at 967.

In general, we are sympathetic to the claim that an authenticated security agreement can be proven by the use of multiple documents, as in the leading case of [*Numeric*]. In that case the person claiming to be a secured creditor was unable to produce a written, signed security agreement. Although he maintained there was such an agreement, all he could produce was a financing statement that listed the collateral and the minutes of the board of directors of the debtor that approved the granting of a security interest. The court concluded that the financing statement satisfied the Statute of Frauds requirement in 9-203 and that the directors' resolution established that an agreement in fact existed to give security. Noting that the UCC should be “liberally construed”, the court found that the secured creditor had proved an enforceable security agreement. Even when there is no fully formed security agreement, in most cases, the loan will be manifest. Notes, payments, and other performance will show it. There will also be considerable evidence of intention to grant security (written inventories of collateral, identification of collateral in one way or another, and filed financing statements). It is likely that a court will read documents together and hold that they satisfy the objective test of 9-203 when they have been executed as part of a whole, they include internal cross references, prior course of dealing indicates they should be read together, the documents include a financing statement, other documents indicate that the parties assumed an unsigned security agreement was in force, course of performance, and testimonial and other nondocumentary evidence shows the parties plainly intended to create a security interest. (Technically, this last factor may not be strictly relevant, for the question is whether the objective writing requirement of 9-203 is satisfied.)

4 James J. White & Robert S. Summers, UNIFORM COMMERCIAL CODE § 31-3 (5th ed., 2004

update). Another commentator provided the following insight.

Although a particular security agreement does not expressly grant or reserve a security interest, it satisfies the requirements of the Code if it recognizes that the creditor has the security interest in the collateral. That is, any language recognizing the existence of a security interest is sufficient and it is not necessary that there be language expressly “granting” a security interest to the creditor. Similarly, it is sufficient to recite that certain personal property is encumbered as security for an obligation. When the seller reserves title until paid, the reservation constitutes a security interest and therefore it is unnecessary for the agreement to expressly state that the seller has or is given a security interest. A promissory note given by the buyer to the lender that recites that upon default the lender has the right to goods purchased by the buyer constitutes a security agreement.

8A Anderson, UNIFORM COMMERCIAL CODE, § 9-203:89 (2004 update). Judge Peterson, in *Ace Lumber Supply*, 105 B.R. at 968, quoting from *In re Murray Brothers*, 53 B.R. 281, 284-85 (Bankr. E.D.N.C. 1985), stated:

The determination of whether a security interest exists is a two-step process. First, the court must determine as a question of law whether the language in the writing required by [9-203] objectively indicates that the parties intended to create a security interest. If the statute of frauds requirement is met, then the factfinder must determine whether the parties actually intended to create a security interest. Parol evidence may be admitted to interpret an ambiguous writing but may not be introduced to satisfy the statute of frauds requirement.

See also *Nationsbank, N.A. v. Outboard Marine Corp. (In re Outboard Marine Corp.)*, 300 B.R. 308, 321-24 (Bankr. N.D.Ill.2003).

In the considering the facts in the case *sub judice* and the instructive commentary and case law referenced above, the Court concludes that under the composite document theory that the promissory note and the financing statement are sufficient, as a matter of law, to create a security interest in Debtor’s personal property described on the financing statement. The promissory note signed by Debtor specifically references that a “[s]ecurity interest will be filed . . . on Form UCC-1 for merchandise delivered to date and security interest shall be retained on

merchandise in storage. . . . [GVF] shall have immediate access to secured merchandise for purpose of recovery of amount due should any payment be not made in a timely manner”

The financing statement, signed contemporaneously with the promissory note, by the Debtor, contains a complete description of personal property.

The Court further concludes, given the contents of the promissory note and financing statement and the testimony of the witnesses, as a question of fact, that Debtor and [GVF] actually intended to create a security through the terms of the promissory note and financing statement. When the Debtor signed the promissory note and the financing statement does not alter the above analysis. The date when the promissory note and financing statement were signed and the corresponding date of attachment and perfection may, but not in this case, have been critical to a trustee’s preference investigation. *See* MCA §§ 30-9A-324(1) (perfection when debtor receives possession or within 20 days thereafter), 30-9A-309(1) (perfection on attachment regarding consumer goods), 30-9A-203(2) (attachment and enforcement when value and rights and powers pass and one of three conditions are met, e.g., authentication; and 11 U.S.C. § 547(c)(3) (exception to avoidance when security interest created and perfected on or before 20 days after debtor takes possession).

While the above identified language in the promissory note is certainly not the best language to use in a security agreement, it clearly provides that GVF is entitled to possession of its collateral in the event Debtor defaults under the terms of the promissory note. The Court thus finds that such language does indeed create and provide for a security interest for [GVF] in the furniture purchased by Debtor from GVF.

Debtor admits that she has not made a payment to GVF since March of 2004. Given the

foregoing and the fact that GVF's collateral is declining in value on a daily basis, the Court finds that cause exists under 11 U.S.C. § 362 to grant GVF its requested relief.

IT IS ORDERED at that a separate order modifying the stay afforded by § 362(a) of the Bankruptcy Code will be issued permitting Gallatin Valley Furniture to proceed with its nonbankruptcy remedies against the following items of property:

Hooker Sleigh Bed, #605-90-286;
Buus Dining Table, #32/08/662;
Hooker Armoire, #605-90-013;
Eurl 41012C Lamp;
Ploi Side Chair (4) #610;
Leathercraft Sofa #H2590;
Leathercraft Chair, #H2602;
Lee Industries Chair (2), #1065;
Habersmith Hutch, #23-2258D;
Jacanan Large Chest #4564LG;
Simmons Baymont Plush King Mattress & Boxspring;
Collin Design Table Lamp (2), #160;
Hooker Single Dresser, #605-90-001;
Hooker Oval Nite Stand, #605-90-017;
Pacific Coast Lighting Table Lamp (2), #87-352-76;
Shadow Catcher Evening in April #7543 Picture;
Shadow Catcher Marsh Side #6260 Picture;
Shadow Catcher Evening River #7543 Picture
Shadow Catcher Canadian Fall #7501 Picture;
Habersham Rio Grande Chest #17-5133A;
Old Java Oval Cocktail Table #CT-01-OSS;
Old Java Rectangular Rustic End Table #ET-07-S; and
Lee Industries Malden Poppy Seed Sectional #20-313LF/101/111/313.

BY THE COURT

A handwritten signature in cursive script, reading "Ralph B. Kirscher", is written over a horizontal line.

HON. RALPH B. KIRSCHER
U.S. Bankruptcy Judge
United States Bankruptcy Court
District of Montana

